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Decision 02-06-068 June 27, 2002

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U-338-E) for Approval of Amendments to Power Purchase Contracts Between Southern California Edison Company and Seven Landfill Gas Biomass Projects (QFIDs 1103-1107, 1110 and 1111).	Application 02-01-018 (Filed January 11, 2002)

OPINION GRANTING APPLICATION FOR QUALIFYING FACILITY CONTRACT EXTENSIONS

In this decision, we grant the unprotested application of Southern California Edison Company (Edison) to extend for five years Standard Offer 1 (SO1) contracts that Edison entered into on November 27, 1996 with seven Qualifying Facilities (QFs) that generate electricity by means of methane gas that is produced and collected at landfills. Six of the seven landfill-powered generating facilities are located in Edison's service territory; one is located outside it.

Because the contract extensions could affect negotiations with other QFs, Edison filed the full terms of the extensions under seal, along with a motion requesting that these terms be kept confidential pursuant to Public Utilities Code Section 583 and General Order (G.O.) 66-C. Edison also filed redacted and unredacted versions of certain exhibits to the application, and requested that the unredacted versions remain under seal. In today's decision we grant Edison's motion in part, but we also conclude that more of the extension terms and

application exhibits can be discussed without harm to Edison or its ratepayers than is assumed in Edison's motion.

Background

As Edison notes in its application, the contract extensions in question are before us because of certain exceptions for landfill biomass QFs that the Commission carved out in D. 96-10-036 (68 CPUC2d 434), the 1996 decision that modified the terms of SO1 contracts in light of the then recently-enacted AB 1890 and the planned deregulation of the electricity market. Although D.96-10-036 (as modified by D.96-11-018) provided that new QF contracts would expire on December 31, 2001 and placed QFs on notice that they could not expect regulatory must-take status if they entered into SO1 contracts after December 20, 1995,[1] the decision also established two limited exceptions to its must-take rule. The first was for QFs that agreed to SO1 contract modifications allowing the

[1] D.96-10-036 reached this conclusion because of the Commission's concerns about the dispatch priority then enjoyed by the holders of SO1 contracts. The decision described the problem as follows:

> "If a generator seeks to compete in the new market as a direct access provider, and other competing generators are able, through the continued availability of the [SO1] for some or all of their capacity, to . . . avoid curtailment, then the number of hours during which minimum load conditions exist will expand to fill the year. Generators' profitability is highly correlated to the magnitude of unplanned outages, as turning a plant on and off increases operations and maintenance costs of the QF and disturbs the steam host's operations. The advantage of obtaining must-take status is viewed as providing a 'right to run' when others are subject to curtailment. This consequence is not the comparable, non-discriminatory access to and use of the transmission grid we require. The number of minimum load hours experienced today with separate control areas for PG&E, SCE, and SDG&E will dramatically swell if a preference relative to other generators in the market can be obtained through the [SO1]." (*Mimeo.* at 43-45.)

output of the QF to be delivered to a direct access customer. The second exception, made for policy reasons, was for "landfill biomass QFs that allow another entity to become eligible for tax credits under Section 29 of the Internal Revenue Code." (*Id.* at 45, n. 22.)[2]

As Edison notes in its application, the policy reasons supporting the exception for landfill QFs "relate[] to the purported societal benefits that are typically identified with QFs of this nature, specifically the use of a renewable fuel that has the subsidiary benefit of preventing or reducing the flaring of potentially harmful methane gas." (Application, p. 4.) The application continues that each of the projects at issue "uses a landfill gas collection system feeding a generator that produces the electricity sold to [Edison]. As noted above, by using the landfill . . . gas to fuel their generators, the Projects do not simply generate electricity from a renewable fuel source; they also avoid or reduce the necessity of flaring of potentially harmful methane gas." (*Id.* at 5.)

The seven SO1 contracts for which Edison is seeking extensions were all entered into on or about November 27, 1996, and all of them provide for an expiration date of December 31, 2001 (subject to extension by the Commission). The Edison contract numbers, location of the landfills, date of first operation and rated capacity of the facilities (net of station use) are set forth in the table below.

[2] In D.96-10-036 as originally issued, footnote 22 described the second exception as applying to "small, publicly owned, landfill biomass QFs." D.96-11-018 modified this language to read as it appears in the text above. (69 CPUC2d 205, 206.) To conform the Commission's policies with AB 1890, D.96-11-018 also provided that unless they were extended, new QF contracts would expire on December 31, 2001 rather than December 31, 2002. (*Id.*)

Contract No.	Location	Operational Date	Nameplate Rating
1103	Visalia	May 8, 1998	1.9 MW
1104	Santa Barbara	August 5, 2000	3.0 MW
1105	Lake View Terrace	January 5, 1999	6.0 MW
1106	Woodland	March 1, 1997	2.45 MW
1107	Tulare	December 17, 1999	1.9 MW
1110	West Covina	October 5, 1996[3]	6.5 MW
1111	West Covina	October 5, 1996[4]	6.5 MW

Summary of Contract Extension Terms

Edison begins its discussion of the contract extension terms by reiterating its view that it was not obliged to renew these contracts "under PURPA, or otherwise," because "the so-called 'societal benefits' attributed to QF projects cannot properly be used to coerce public utilities into making purchases from QFs that they are not obligated to make." Rather, Edison continues, it viewed its negotiations with the landfill projects' owners as voluntary, and made it clear to the owners that Edison would not agree to contract extensions unless it obtained "terms and conditions that offered ratepayer benefits and protections." (Application, p. 12.)

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[3] According to the application, Contract 1110 was entered into with a pre-existing facility, and so was deemed to have achieved firm operation on the contract's starting date. However, the facility was out of service for an extended period because of turbine problems, and did not return to service until April 1999. (Application, p. 8.)

[4] The application states that like the project covered by Contract 1110, this facility is located at the BKK Landfill in West Covina, California. It also pertains to a pre-existing facility and so had an operational date that coincided with the contract's starting date. Unlike Contract 1110, however, this project has not been out of service for an extended period. (*Id.* at 9.)

For the following reasons, Edison concludes that such ratepayer benefits and protections have been achieved in the contract extensions at issue:[5]

> ". . . SCE concluded that the energy pricing terms agreed to for the extension period would likely produce cost benefits when compared to probable market rates. In addition, the fixed pricing aspect during the first ** months of the Amendments will provide 'hedging' value against potentially volatile 'avoided cost' rates that could arise if natural gas markets were again to experience the instability that was demonstrated in the latter part of 2000 and early 2001. Finally, SCE's ability to exercise an early termination after ** months into the new, extended term[6] provides significant protection should it turn out that the fixed prices have become non-cost effective or if it is ascertained that the as-available capacity provided by Seller is no longer needed because of minimum load conditions, or otherwise." (*Id.* at 12-13.)

Edison is convinced that the fixed price terms it has negotiated for the first part of the contract extension are reasonable in relation to what gas prices are expected to be during that time period:

> "As to the cost-effectiveness of the agreed-to energy prices, the fixed rates provided for during the first ** months of the extended Contract term (***) are projected to be between 66% and 97% of the price that SCE would pay if it had to procure the same amount of electricity from an alternative source, as described briefly below and in more detail in Exhibit SCE-4. For the remainder of the Contracts' terms, Sellers will receive ***." (*Id.* at 13.)

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[5] In the quotation in the text, the asterisks indicate the material we have redacted from Edison's non-public version of the application, which was filed under Pub. Util. Code § 583. Our redactions are slightly less extensive than those contained in the public version of the application that Edison filed.

[6] While the precise terms of these termination privileges will remain under seal, we can state that Edison has rights to terminate the contract extensions without penalty even during the fixed-price period of the extensions.

This conclusion is based upon an analysis of three different measures of the replacement price that Edison believes it would have to pay for energy from alternative sources. This analysis is presented in the prepared testimony of Richard B. Davis (which Edison has filed in both unredacted and redacted versions) and is summarized in the application as follows:

> "The first approach was to ascertain a likely future South Path 15 ('SP15') market price based on a recent (***) broker quote for SP15 from Natsource LLC. The average fixed energy price that would be payable to Sellers under the Amendments is projected to be approximately 97.4% of the average SP15 price obtainable from the quoted source over the same period.
>
> "The second SP15 price measure used Topock gas price data from the *** gas forecast by Data Research Inc. ('DRI'), coupled with an assumed heat rate, gas intrastate transportation price and 'spark spread.' The spark spread (in cents/kWh) is a measure of the price of construction and operation of a gas-fired project excluding fuel. The average energy price (over ** months) that would be payable to Sellers under the Amendments is projected to be approximately 72% of the SP15 price developed in this manner.
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> "The third SP15 price measure SCE consulted is NYMEX gas price data from *** and ***, as reported in the *Wall Street Journal*, coupled with an assumed heat rate, gas intrastate transportation price, and spark spread. The average price (over ** months) that would be payable to Sellers under the Amendments is projected to be 66% of the SP15 price developed in this manner." (*Id.* at 13-14; footnotes omitted.)

Discussion

After reviewing both the public and non-public versions of Edison's filings, we conclude that the contract extensions with the seven landfill QFs are reasonable, and we approve them.

Our principal reason for doing so is that under the extensions, Edison is obliged to pay fixed energy prices for only a limited period, and it may terminate

the contracts without penalty after a certain time has elapsed even within the fixed-price period.

Although we agree with Edison that the fixed energy price it has agreed to pay should remain under seal pursuant to Pub. Util. Code § 583 and G.O. 66-C, we can state that this price is below the 5.37 cent per kilowatt-hour benchmark that we established last year in Decision (D.) 01-06-015. In that decision, in order to encourage maximum energy production by QFs in the hope of averting blackouts during Summer 2001, we ruled that amendments between QFs and the three major investor-owned utilities that (1) were entered into by July 15, 2001, and (2) substituted a fixed, five-year energy price of 5.37 cents per kilowatt-hour (kWh) for Short Run Avoided Cost (SRAC) energy payments, would automatically be deemed reasonable. In D.01-09-021, we extended the "safe harbor" deadline for deeming such amendments reasonable to July 31, 2001.

However, due in part to the significant fall in gas prices between June and September 2001, we subsequently declined to extend any further the date for deeming such contract amendments reasonable. In D.01-10-069, for example, after noting that "no one can accurately predict what gas prices will be over the next five years," we declined to grant Edison's petition to extend the safe harbor date for QF contract amendments to September 6, 2001. We characterized the decisions after D.01-06-015 as clearly demonstrating "that the Commission was cognizant of changing market conditions, and did not want to deem reasonable contract amendments entered into after a certain date. The recent drop in gas prices reflects a change in market condition, and the utilities and QFs should [now] seek approval of these amendments through the application process rather than have the amendments automatically deemed reasonable." (*Mimeo.* at 12.)

Gas prices now are slightly higher than in Fall 2001, but the fixed energy price that Edison has agreed to pay the landfill QFs during the first part of the

contract extension term is reasonable in relation to them. Moreover, as noted above, Edison has a right to terminate the contract without penalty after a certain point during the fixed-price period, so we agree with Edison that its "ability to exercise an early termination . . . provides significant protection should it turn out that the fixed prices have become non-cost effective or if it is ascertained that the as-available capacity provided by Seller is no longer needed because of minimum load conditions, or otherwise." (Application, p. 13.) We also agree with Edison that the pricing terms it has agreed to for the remainder of the contract extension (which terms Edison has filed under seal) are reasonable.

Two issues remain. The first issue is whether we should grant Edison's request for a finding that "all payments to be made to Sellers by [Edison] under the Contracts, as amended by the Amendments, are reasonable and prudent and recoverable in full by [Edison] through rates or such other cost recovery mechanism as the Commission may authorize, subject only to [Edison's] prudent administration of the Contracts, as amended by the Amendments." (*Id.* at 18.)

This request for approval of payments to be made under the contract extensions is reasonable, and consistent with language we have used in other, recent decisions approving amendments to QF contracts and settlements with QFs. In Ordering Paragraph (OP) 3 of D.01-06-015, for example, we held that under the three QF contract amendments deemed reasonable if entered into by July 15, 2001, the three investor-owned utilities should "be authorized to recover all reasonable payments made under the contracts subject to their prudent administration of the amendments." (*Mimeo.* at 11.) Similarly, OP 2 of D.02-04-014 authorized Edison to recover in rates all prudently-made payments

to a QF, NP Cogen, with which Edison had recently entered into a settlement agreement. (*Mimeo.* at 10.)[7]

The second remaining issue -- one on which we feel obliged to express our disapproval -- is Edison's recent practice of insisting in QF contract extensions and settlements that the Commission take action by a certain date, or the amendment or settlement will be deemed null and void. In this case, for example, each of the seven original contract amendments required the Commission to issue a decision "approving the Amendment in its entirety, without conditions or modifications unacceptable to either Party, that has become final and is no longer subject to appeal and which contains the Required Findings," no later than April 30, 2002.[8] Since a Commission decision is not normally considered final and no longer subject to judicial review until both the 30-day period for seeking rehearing and the 30-day period for seeking judicial review have passed, this language seemed to mean that the parties expected the Commission to issue a decision approving the amendments no later than

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[7] D.02-04-014 also noted that the proper accounting vehicle for recovery of the settlement payments was the Annual Transition Cost Proceeding (ATCP) or its successor mechanism. We described the ATCP as follows:

> "The ATCP was established in D.97-06-060 as part of the establishment of the transition cost balancing accounts. The reasonableness of the QF contract administration is to take place in the ATCP, to the extent that such reviews have not been eliminated by the standard offers or other approved contracts." (*Mimeo.* at 7; footnotes omitted.)

[8] In amendments entered into on April 29, 2002, the parties acknowledged that this deadline could not be met and extended the deadline for a final and non-appealable Commission decision to August 26, 2002.

February 21, 2002, less than a week after expiration of the 30-day period for protesting the application.[9]

Including such a limitation in an application is unreasonable, and in certain contexts is contrary to our rules. For example, Rule 51.1(d) states that stipulations and settlements "should ordinarily not include deadlines for Commission approval."[10] Notwithstanding this rule, Edison included a deadline for Commission action in its settlement agreement with NP Cogen.[11] In D.01-10-069, one of Edison's arguments for extending the July 31 "safe harbor" date to September 6, 2001 was that some of the standard QF contract amendments it had negotiated after July 31 "terminate automatically if the Commission does not approve them by certain prescribed dates." (*Mimeo.* at 4.) These passages show that Edison's decision to include a "drop dead" date for Commission action in the contract extensions here was not an aberration, and Edison's attempt to apply unnecessary time pressure, if acceded to, could result in inadequate review of applications.

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[9] Notice of the filing of this application did not appear in the Commission's Daily Calendar until January 17, 2002. Under Rule 44.1 of the Rules of Practice and Procedure, protests to applications must ordinarily be filed within 30 days of such notice.

[10] Rule 51.1(d) also provides that in the "rare case" where delay beyond a certain date would "invalidate the basis for the [settlement] proposal," the timing urgency should be "clearly stated and fully justified" in the motion seeking approval of the settlement.

[11] This is clear from footnote 3 of D.02-04-014, the decision approving the NP Cogen settlement. That footnote states:

> "The Settlement Agreement provides it shall terminate by January 25, 2002, if 'Commission Approval' as defined in the agreement is not obtained or waived by Edison by that date. Edison proposed a 15-day extension to February 9, 2002, a date that has passed." (*Mimeo.* at 4, n. 3.)

While we are approving these contract extensions because they appear favorable to ratepayers, we place Edison on notice that we will look with strong disfavor in future applications on "drop dead" provisions like those quoted above.

Waiver of Comment Period

As noted above, this is an uncontested matter, and the draft decision of the Administrative Law Judge grants the relief requested. Accordingly, pursuant to Rule 77.7(f)(2), the usual 30-day period for public review and comment on the draft decision is being waived.

Findings of Fact

1. Notice of the filing of this application appeared in the Commission's Daily Calendar on January 17, 2002.

2. No protest has been filed to the application, and a hearing is not necessary.

3. Under the terms of the SO1 contracts entered into by Edison with the seven landfill QFs covered by this application, the contracts expire on December 31, 2001 unless extended by order of the Commission.

4. Each contract extension included in Exhibit SCE-2 to the application contains substantially identical terms.

5. There is a benefit to renewing SO1 power purchase contracts with landfill QFs on reasonable terms and conditions, because such QFs use methane gas, a renewable fuel that can be harmful to the environment if flared unnecessarily.

6. The fixed energy price that Edison has agreed to pay the seven landfill QFs covered by this application during the first part of the five-year contract extension is significantly below the 5.37 cents/kWh price that was approved as a substitute for SRAC energy payments in D.01-06-015.

7. The fixed energy price that Edison has agreed to pay the seven landfill QFs covered by this application during the first part of the five-year contract

extension is less than the gas-based, forecasted prices Edison would have to pay to acquire energy on equivalent terms and conditions during the same period.

8. Edison has a right, after a certain point during the fixed-price period, to terminate without penalty the contract extensions with the seven landfill QFs at issue here.

9. The pricing terms in the contract extensions that will apply after the end of the fixed-price period are reasonable.

10. In applications concerning settlements and contract extensions negotiated with certain QFs, Edison has included provisions requiring Commission approval within an unreasonably short time frame.

Conclusions of Law

1. Edison's January 11, 2002 motion to file under seal the unredacted versions of the application and of Exhibits SCE-2 and SCE-4, and also to accept for filing a public version of the application and of Exhibit SCE-4, should be granted to the extent set forth herein.

2. The contract amendments set forth in Exhibit SCE-2, as amended on April 29, 2002, should be approved as reasonable.

3. Edison should be authorized to recover in rates (or such other cost recovery mechanism as the Commission may prescribe) all payments made pursuant to the contract amendments described in Conclusion of Law (COL) 2, subject only to Edison's prudent administration of said amendments and of the underlying contracts.

4. This order should be effective immediately.

O R D E R

IT IS ORDERED that:

1. The contract amendments set forth in Exhibit SCE-2, as amended on April 29, 2002 and covering those contracts identified by Southern California Edison Company (Edison) as QFID 1103, 1104, 1105, 1106, 1107, 1110 and 1111, are hereby approved as reasonable.

2. Edison's January 11, 2002 motion to file under seal the unredacted versions of the application and of Exhibits SCE-2 and SCE-4, and also to accept for filing a public, redacted version of the application and of Exhibit SCE-4, is granted to the extent set forth in this decision. The aforesaid unredacted documents shall remain under seal for a period of two years from the mailing date of this decision, and during that period shall not be made accessible or disclosed to anyone other than Commission staff except upon the further order or ruling of the Commission, the Assigned Commissioner, the assigned Administrative Law Judge (ALJ), or the ALJ then designated as Law and Motion Judge. If Edison believes that further protection of these unredacted documents is needed after two years, it may file a motion stating the justification for further withholding of the material from public inspection, or for such other relief as the Commission rules may then provide. Such a motion shall be filed no later than 30 days before the second anniversary of the mailing date of this decision.

3. Edison is hereby authorized to recover in rates (or such other cost recovery mechanism as the Commission may prescribe) all payments made pursuant to the contract amendments described in Ordering Paragraph 1, subject only to Edison's prudent administration of said amendments and of the underlying contracts.

This order is effective today.

Dated June 27, 2002, at San Francisco, California.

LORETTA M. LYNCH
President
HENRY M. DUQUE
CARL W. WOOD
GEOFFREY F. BROWN
MICHAEL R. PEEVEY
Commissioners